



Guideline

Sales Tax Freight, Delivery & Other Transportation Charges

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In general, the taxability of freight, delivery and other transportation charges depends on the terms of the sale and how the goods are delivered. Freight, delivery and other transportation charges are taxable if title (or ownership) to the merchandise does not pass from the seller to the buyer until delivery is made. They are not taxable if title to the merchandise passes at the point of origin and delivery is made by a licensed common carrier. To determine whether freight, delivery and other transportation charges are subject to North Dakota sales tax, all of the factors below must be considered:

1. When does title (or ownership) pass to the buyer?
2. What are the terms of each sale?
3. How is delivery made by the seller?
4. What is the conduct (actions) of the buyer and the seller compared to the terms of the sale?
5. Was the merchandise in existence and clearly identifiable?
6. Was the seller required to do something to put the merchandise into a deliverable or sellable state?
7. What are the common business practices in the trade or industry of the seller?

When Does Title Pass to the Buyer?

The most important factor in determining whether freight, delivery and other transportation charges are taxable is the point where title (or ownership) to the merchandise transfers from the seller to the buyer. Freight, delivery and other transportation charges are subject to sales or use tax if title does not pass to the buyer until delivery is made. In other words, if the buyer and the seller agree that title to the merchandise does not pass to the buyer until delivery then the freight, delivery and other transportation charges are always taxable. If the buyer and the seller agree that title to the merchandise passes to the buyer before delivery and delivery is provided by a licensed common carrier, then the freight, delivery and other transportation charges are not subject to sales tax.

If no clear agreement exists between the seller and the buyer as to when title passes, title is presumed to pass when delivery is made and all freight, delivery and other transportation charges are subject to sales tax. The best agreement is a written contract signed by both the seller and the buyer that states when title passes from the buyer to the seller. If no written contract exists, then the transaction will be considered according to:

1. The stated terms of the sale, as shown on the invoice.
2. The understanding and actions of both the seller and the buyer.
3. Who delivered the merchandise?
4. Was the merchandise in existence and clearly identifiable?
5. Did the merchant have to do something to the merchandise to put it in a final, sellable or deliverable state?

As you can see, the fact that an invoice has been marked *f.o.b. point of origin* or *source of supply* is not necessarily controlling if the other factors are missing. For example, if the invoice is written with the terms of the sale quoted as *f.o.b. source of supply* but the seller remains liable for the merchandise until delivery is made, it is clear that the conduct (actions) of the parties to the sale is in conflict with the stated terms of the sale, and the freight, delivery and other transportation charges in this case are taxable. Another example might be a ready mix company selling ready mixed cement to a customer and having its invoices marked *f.o.b. plant*. Since the common business practice in this industry is to sell at a delivered price, the stated terms of the sale are in conflict and the commonly accepted business practice would control; therefore, the freight, delivery and other transportation charges would be considered taxable. Please see the paragraphs below for a detailed discussion of these factors.

Terms of the Sale

As indicated above, the terms of the sale control the taxability of freight, delivery and other transportation charges **except** where other factors are in conflict with the stated terms. If the stated terms on the invoice or sales agreement are *f.o.b. source of supply*, then the conduct (actions) of both the seller and the buyer must be consistent with those terms. Each must have a clear understanding of the terms of the sale, the merchandise must be in existence and be identifiable and the terms must conform to the common business practices in the trade or industry of the seller.

If the terms of the sale are *f.o.b. source of supply*, any claims for freight damage must be prepared and submitted by the buyer since the merchandise legally belongs to the buyer and is the responsibility of the buyer during delivery. A freight claim filed by the seller indicates that the seller is still responsible for the merchandise and is in conflict with the stated terms of the sale.

If there is no written contract or agreement setting out title passage, then the invoice should be marked to indicate the terms. If no written contract or agreement exists and if the invoice or sales agreement does not state the terms of the sale, the sale is completed upon delivery of the merchandise and any freight, delivery and other transportation charges are taxable.

Delivery by the Seller

North Dakota sales and use tax law provides for an exemption for freight when the transportation service is provided by a licensed common carrier and title to the transported tangible personal property has passed from the seller to the purchaser.

It is important to note this transportation service must be provided by a licensed common carrier in order for the exemption to apply. Charges for deliveries made in the retailer's vehicle **always** are subject to tax even though the delivery charges may be itemized separately from the goods being sold.

Conduct of Both Parties to the Sale

The actions of the seller and the buyer must be consistent with the stated terms of the contract for the sale. If the terms of the sale are *f.o.b. source of supply*, then the buyer has legally taken title to the goods before delivery. If those goods are lost, damaged or destroyed during delivery, the buyer is responsible for their loss and for filing any freight claims to recover such loss. Should the seller make the freight claim or otherwise act as the owner of the goods, it will be considered as conduct inconsistent with the stated terms of the sale and may result in a determination that the freight, delivery and other transportation charges are subject to sales tax. Both the seller and the buyer must understand and abide by the terms of each sale.

Merchandise Must be in Existence and Clearly Identifiable

In order for a sale to take place, the merchandise being sold must be in existence and must be clearly identifiable. The sales contract or sales agreement must clearly show a serial number or other identifying information which will confirm the existence of a specific item of merchandise or piece of goods. Title cannot pass to the buyer unless there are specific, identifiable goods in existence.

A sales invoice to sell a tractor for future delivery, for example, is not a sale of that tractor unless a specific tractor with an identifying serial number has been set out on that invoice. Freight charges are taxable unless the sale of a specific item of merchandise or a specific piece of identifiable goods is listed on the sales contract or invoice.

Example: Farmer A wants to buy a tractor late in the year to take advantage of the depreciation for that year's income taxes. Implement dealer B has no such tractor available for sale but offers to order one for spring delivery. The farmer agrees and executes a purchase agreement with the implement dealer in which the farmer agrees to purchase a certain tractor for \$50,000.00 plus the freight, delivery and other transportation charges from the factory. The farmer pays the implement dealer \$50,000.00. Since there is no specific, identifiable tractor in existence at the time no sale has been made. The implement dealer should simply credit the farmer with a \$50,000.00 deposit and should not report or pay sales tax on the sale of that tractor. The farmer cannot report the purchase of a tractor for income tax purposes.

On April 1, the implement dealer is notified by the factory that the tractor has been built and will be shipped on April 10. The factory gives the dealer a description of the tractor including the serial number. At this point, the implement dealer may prepare an invoice selling that specific serial numbered tractor to Farmer A. If the sales agreement between the implement dealer and the farmer states that the terms of the sale are *f.o.b. factory*, and the tractor is transported by a licensed common carrier, then the freight, delivery and other transportation charges are not subject to sales tax. If the sales agreement does not indicate the terms of the sale, then it is presumed title to the tractor passes to the farmer-buyer upon actual delivery and in that case, the freight, delivery and other transportation charges from the factory are subject to sales tax.

Incoming Freight and Service Work

Charges paid by a retailer for the transportation of tangible personal property from the source of supply to the retailer's place of business are not deductible for sales tax purposes by the retailer from the price for which the goods are sold. When a retailer purchases goods for inventory, the freight, delivery and other transportation charges from the wholesaler are always included in the final sales price that the retailer's customer subsequently pays for those goods.

If the dealer must do something to the merchandise to put it into a deliverable or sellable state, transfer of title to the merchandise cannot occur before that act; therefore, freight, delivery and other transportation charges incurred prior to that act are subject to sales or use tax. Freight, delivery and other transportation charges which occur after that act may or may not be taxable, depending upon the terms of the sale and the understanding of both the seller and the buyer.

Example: Implement dealer A orders a new tractor for Farmer B. Farmer B specifies that a front end loader be attached to that tractor and pays the implement dealer for the entire unit. The title to the tractor will not pass to the farmer until such time that the implement dealer has received the tractor from the factory and has attached the front end loader. Freight and delivery charges from the factory are subject to tax since something remained to be done to the goods before they were in a sellable or deliverable state.

Common Business Practices

There are certain business establishments which almost always deliver the merchandise they sell. These include sand and gravel dealers, ready mix cement dealers, coal and lumber dealers and others. Since the common business practice of these industries is to deliver the products they sell, freight, delivery and other transportation charges are subject to sales tax even if set out separately. Terms of such sales cannot be *f.o.b. source of supply*, since the freight, delivery or other transportation charges are considered part of the selling price of the merchandise. Sales of sand, gravel or ready mix cement are rarely made without the element of delivery.

Recap

Freight, delivery and other transportation charges including postage, UPS charges, bus charges, railway express charges, air, freight and all others are included in the base upon which sales or use tax is charged unless all of the following conditions are present:

1. The terms of the sale were *f.o.b. point of origin*.
2. Both the seller and the buyer agreed that the terms were *f.o.b. point of origin*.
3. There was a written agreement specifying that title (or ownership) to the goods passed at the point of origin.
4. The seller did not deliver the merchandise in his own delivery equipment.
5. Conduct (actions) of both the seller and the buyer indicated that both clearly understood the terms of the sale.
6. The merchandise being sold was in existence and was clearly identifiable.
7. Nothing remained for the seller to do to put the merchandise into a deliverable state.
8. The common practice of the business or trade of the seller did not conflict with the terms of the sale.